

Private Letter Ruling: Exempt organizations described in IITA Section 205(a) do not add back their federal net operating loss deductions and are not entitled to an Illinois net loss

October 25, 1999

Dear:

This is in response to your letter dated October 5, 1999, in which you request a Private Letter Ruling on behalf of xxxxxxxx xxxxxxxx xxxxxxxxxxxx xx xxxxxxxx. Review of your request for a Private Letter Ruling disclosed that all information described in paragraphs 1 through 8 of subsection (b) of the enclosed copy of Section 1200.1120 appears to be contained in your request. The Private Letter Ruling will bind the Department only with respect to xxxxxxxx xxxxxxxx xxxxxxxxxxxx xx xxxxxxxx for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither xxxxxxxx xxxxxxxx xxxxxxxxxxxx xx xxxxxxxx nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

The facts and analysis as you have presented them are as follows:

We received the enclosed taxpayer notification proposing an adjustment to the September 30, 1998 tax return IL 990-T. You have used Section 205(a) as your reason for the change.

We take exception to Section 205(a). Section 205(a) describes a Not for Profit tax exempt corporation having income not eligible of the net operating loss carryover. The xxxxxxxx xxxxxxxx xxxxxxxxxxxx xx xxxxxxxx Not for Profit Tax exempt corporation also has income required to be reported on form 990-T subject to Federal and State income tax. The net operating loss carryover is available to a taxed entity as described in Illinois Section 203. The Section allows the use of a Net Operating Loss carryover against the taxable portion as reported on form IL 990-T.

Your reasoning and position concerning this matter does not reflect the Federal rules for the application of a net operating loss carryover. Also Form IL 990-T clearly indicates on Page 1 Part III, Line 1B "Enter the Net Operating Loss" from form NLD for carryback periods. I have enclosed the copy of IL Form 990-T as filed for 9/30/98.

Please abate the balance due of \$3,583.35, adjust your records accordingly and advise of the abatement.

### **Ruling**

The 1997 Form IL-990-T that xxxxxxxx xxxxxxxx xxxxxxxxxxxx xx xxxxxxxx properly used to report its Illinois income tax liability for its taxable year ending September 30, 1998, provided that the taxpayer should begin its computation of base income with its unrelated business taxable income properly reported for federal income tax purposes, without reduction by any federal net operating loss deduction. That form also provided that the taxpayer was entitled to an Illinois net loss deduction.

Section 205(a) of the Illinois Income Tax Act (the "IITA"; 35 ILCS 5/101 et seq.) provides:

The base income of an organization which is exempt from the federal income tax by reason of Section 501(a) of the Internal Revenue Code shall not be determined under section 203 of this Act, but shall be its unrelated business taxable income as determined under section 512 of the Internal Revenue Code, without any deduction for the tax imposed by this Act. The standard exemption provided by section 204 of this Act shall not be allowed in determining the net income of an organization to which this subsection applies.

The only provisions in the IITA that deny a taxpayer the benefit of a net operating loss deduction properly claimed for federal income tax purposes are contained in Section 203(b)(2)(D) (for corporations) and Section 203(c)(2)(D) (for trusts and estates). Because Section 205(a) of the IITA expressly provides that Section 203 of the IITA does not apply to the computation of base income of an exempt organization, the provision in the 1997 Form IL-990-T requiring the taxpayer to add back its federal net operating loss deduction is erroneous.

Section 207(a) of the IITA (as in effect prior to the enactment this year of Public Act 91-541, and thus as applicable to xxxxxxxx xxxxxxxx xxxxxxxxxxxx xx xxxxxxxx taxable year ending September 30, 1998) provided:

If after applying all of the modifications provided for in paragraph (2) of Section 203(b), paragraph (2) of Section 203(c) and paragraph (2) of Section 203(d) and the allocation and apportionment provisions of Article 3 of this Act, the taxpayer's net income results in a loss, such loss shall be allowed as a carryover or carryback deduction in the manner allowed under Section 172 of the Internal Revenue Code.

Because modifications in Section 203 of the IITA have no application to taxpayers governed by Section 205(a) of the IITA, such taxpayers can have no Illinois net loss carryovers under this provision. Accordingly, the provision in the 1997 Form IL-990-T allowing a taxpayer to claim an Illinois net loss deduction was erroneous.

In summary, the proper method for an exempt organization to compute its net income would be to start with its federal unrelated business taxable income (as reduced by any net operating loss deduction properly allowable for federal income tax purposes) and would not allow any Illinois net loss deduction.

Section 4 of the Taxpayers' Bill of Rights Act (20 ILCS 2520/4) provides, in part:

The Department of Revenue shall have the following powers and duties to protect the rights of taxpayers:

\* \* \*

(c) To abate taxes and penalties assessed based upon erroneous written information or advice given by the Department.

Under this provision, any additional tax or penalty assessed against xxxxxxxx xxxxxxxx xxxxxxxxxxxx xx xxxxxxxx because it followed the erroneous provisions of the 1997 Form IL-990-T must be abated. Accordingly, the notification sent to xxxxxxxx xxxxxxxx xxxxxxxxxxxx xx xxxxxxxx, dated September 7, 1999, is rescinded

and the additional tax, penalty and interest of \$3,583.35 shown on that notification is abated.

Note, however, that xxxxxxxx xxxxxx xxxxxxxxxxxxxx xx xxxxxxxx is not bound to compute its Illinois net income using the erroneous method prescribed in the 1997 Form IL-990-T. If computing its Illinois net income properly -- that is, by neither adding back its federal net operating loss deduction nor claiming an Illinois net loss deduction - would reduce the tax liability of xxxxxxxx xxxxxx xxxxxxxxxxxxxx xx xxxxxxxx for its taxable year ended September 30, 1998, or for any previous taxable year for which the statute of limitations for refund claims has not expired, xxxxxxxx xxxxxx xxxxxxxxxxxxxx xx xxxxxxxx is entitled to file a refund claim for the overpayment.

The facts upon which this ruling are based are subject to review by the Department during the course of any audit, investigation or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

Very truly yours,

Paul Caselton  
Deputy General Counsel -- Income Tax